

# Business Weekly

## Well on the road to recovery



### This Week

A slew of key domestic data is released this week, which will shed further insight into how this recovery is evolving. In particular, we expect GDP data this Thursday to show the economy grew by 0.5% over the March quarter, thus marking the fourth quarter of economic expansion. This follows fifteen months of recession, which saw the NZ economy contract by 3.4%.

There has been increasing signs of the economic recovery becoming more broad-based in recent months. The ex-primary manufacturing and construction sectors, which had borne the brunt of the recession, are expected to show steady growth as demand recovers. Confidence in the manufacturing sector has improved substantially from very weak levels, aided by robust growth in Australia and the low NZD/AUD over early 2010. Meanwhile, consent issuance points to continued recovery in residential construction.

The wholesale and retail trade sectors are also expected to record modest improvement, although activity remains subdued. Weak wage growth has weighed on household spending over the past year. Whilst the recovery in the household sector has not been as convincing as that in other areas to date, stronger demand for labour should encourage households to open their wallets over the coming quarters. In the near term, we expect greater volatility in retail sales figures as households bring forward their purchases of big-ticket items ahead of the GST increase on 1 October.

Signs of a self-sustaining recovery taking shape can also be seen in the substantial improvement in business confidence. Businesses are now confident enough about the recovery in demand that they have begun to expand their available capacity, as reflected in the sharp improvement in investment and hiring intentions.

This rebound in household and business spending is expected to boost import volumes over the coming year. The recession in NZ had triggered a sharp drop in import demand, which has meant an improvement in the current account. Against the backdrop of subdued import demand has been higher export earnings, reflecting stronger commodity prices. Although the drought in the top of the North Island is likely to have put a dent in dairy production, overall export volumes are expected to have fared well early this year.

The RBNZ will be pleased with the export-led nature of the recovery taking place. Recent communications out of the RBNZ have reiterated its desire to see further rebalancing in the economy. This rebalancing will be an important factor in the sustainability of the recovery in the NZ economy. We expect the broadening recovery will give the RBNZ confidence to continue with its monetary policy normalisation by lifting the OCR steadily in 25 basis point increments over the coming year.

### Click here for:

- [Foreign Exchange](#) • Positive sentiment sees NZD post gains on all the main cross rates monitored.
- [Interest Rates](#) • Quiet week as NZ interest rates remain supported following OCR increase.
- [Week Ahead](#) • Credit Card Spending, Current Account, GDP and Merchandise Trade Balance.
- [Week in Review](#) • REINZ housing, Consumer Confidence, Tourism and Migration.
- [Global Calendars](#) • US housing data, FOMC rate decision, Bank of England Minutes.

### Chart of the week



- Recent consumer confidence surveys have shown a substantial increase in the number of households who consider now as being a good time to purchase a major household item.
- The last GST increase in 1989 saw durable goods sales volumes increase around 10% in the quarters prior to the GST increase. This increase was followed by a sharp decline in durable goods volumes in the subsequent quarter.
- We expect households will once again bring forward purchases of big-ticket items over the coming months, ahead of the GST increase on 1 October.
- However, the increased prevalence of sales promotions now may mean this bringing forward of purchases will occur to a lesser extent.

### General Advice Warning

As this report was prepared without taking into account your objectives, financial situation or particular needs, you should not take any action in reliance of this report without considering your particular circumstances and, if necessary, obtaining professional advice.

## Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	6 mths ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.7118	0.6921	0.6731	0.7098	0.6384	FLAT	0.7000	0.7250
NZD/AUD	0.8095	0.8085	0.8110	0.7988	0.7962	FLAT	0.8000	0.8150
NZD/JPY	64.50	63.61	60.61	64.11	61.62	FLAT	63.00	66.00
NZD/EUR	0.5734	0.5684	0.5329	0.4944	0.4587	FLAT	0.5700	0.5800
NZD/GBP	0.4798	0.4737	0.4669	0.4394	0.3907	FLAT	0.4750	0.4850
TWI	68.2	67.3	65.1	64.8	60.5	FLAT	67.5	69.0

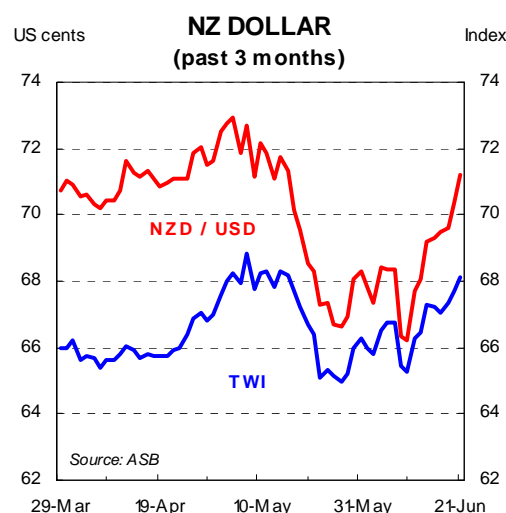
^Weekly support and resistance levels \* Current is as at 10.00 am Monday; week ago as at Monday 5pm

- The NZD lifted last week, buoyed by improving global sentiment. This week the focus is on the Q1 GDP report. Both our own forecast and the median market expectation is for a 0.5% expansion during the quarter. The ongoing NZD recovery, combined with confidence offshore should help the NZD. However, the kiwi is likely to meet some resistance around the 0.720-0.725 level.
- The AUD and NZD received a boost this morning following reports by the People's Bank of China that they will relax their 22-month 'steady state' policy for USD/CNY. We believe the news from China will push Europe's problems into the background for now.
- Providing a downside risk for the AUD and NZD this week is the Federal Reserve meeting. The Fed is likely to reiterate that rates will stay low for an extended period after its policy meeting on Thursday morning NZT. We place a 30% chance that the Federal Reserve modifies its 'extended period' comment. If the Federal Reserve does modify the language in its statement, the USD is likely to rise across the board.
- We expect the majority of the US economic data scheduled for release this week to indicate the economic recovery is on track, further supporting the USD.

### Short-term outlook:

Key data	Date	Time (NZST)	Market expects
Q1 Current Account	23/6	10.45 am	-2.7%
Q1 GDP	24/6	10.45 am	0.5%
May Merchandise Trade	25/6	10.45 am	+835
NBBO Business Outlook	28/6	3.00 pm	-

**Potential currency movers from offshore this week:** Euro current account, US existing home sales, house prices, Richmond manufacturing survey (22nd); Bank of England Minutes, Fed policy decision, US new home sales (23rd); durable goods orders, jobless claims (24th); consumer confidence (25th). Speeches: nil.



### Medium-term outlook: [\[Last Quarterly Economic Forecasts\]](#)

- The USD has firmed slightly earlier than we had previously anticipated. We expect the USD will continue to gain support. The US economic outlook continues to improve, with recent data demonstrating a broader-based expansion. We expect that US bond yields will eventually adjust higher reflecting the firmer US economy. As a result, the higher US bond yields will support the USD. In addition, the AAA-rated US bond market remains the major alternative to the Eurozone government bond market.
- We have already revised down our EUR forecasts three times this year, and recently revised down the outlook once again for the same reasons. Eurozone GDP growth is expected to under perform the US economy over 2010 and 2011. The deterioration in the EU growth outlook will see the differential between US and Eurozone interest rates widen, reducing support for the Euro. In addition, more than half of Eurozone government debt is no longer AAA rated, with uncertainty continuing to cloud the outlook and reducing investor appetite.
- While we have revised down our NZD outlook slightly, we continue to see support coming from strong commodity prices and the RBNZ tightening cycle. In addition, NZ's relatively healthier outlook for net government debt will make the NZD look favourable relative to European and US peers.
- Relative to the AUD, the NZD has already made up quite a bit of ground. The NZD is likely to continue to modestly outperform the AUD as the RBNZ continues to lift rates and the interest rate differential narrows slightly.

## Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	2.75	2.75	2.50	2.50	2.50	FLAT
90-day bank bill	3.11	3.08	2.89	2.76	2.81	UP
2-year swap	4.35	4.35	4.33	4.56	3.96	UP
5-year swap	5.09	5.06	5.24	5.55	5.46	UP
5-year benchmark gov't stock	4.87	4.88	4.97	5.43	4.93	UP
NZSX 50	3048	3041	3050	3150	2788	UP

\* Current is as at 10.00 am Monday; week ago as at Tuesday 5pm. Please note that we have recently changed the NZ gov't 5-year benchmark bond to April 2015 maturity (from April 2013). This does cause some distortion in the comparison against the previous levels (i.e. month ago).

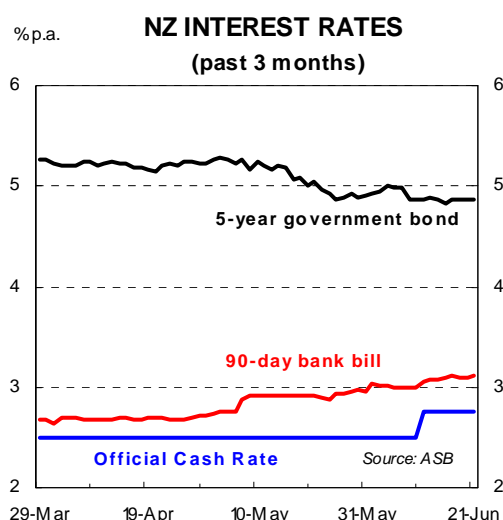
- The NZ market was relatively quiet, with a lack of data to provide direction. Interest rates have been generally well supported following the OCR increase by the RBNZ on June 10. Markets currently have 84% chance of a 25 basis point follow up hike priced in for July. We expect the RBNZ will continue to lift the OCR in a steady fashion (i.e. 25bp a meeting), barring a substantial deterioration in funding conditions.
- While short-term rates have lifted over the past few weeks, on the back of the OCR hike, longer-term interest rates have remained subdued, resulting in the yield curve flattening. In particular, government bond yields remain low, weighed by offshore concerns on Europe and weak investor appetite for risk.
- US Government Treasury yields failed to make a recovery last week, despite the recovery in risk appetite which tends to reduce demand and increase yield on US Treasury bonds. In particular, yields eased on Friday, as investors moved to square up positions ahead of this week's bond auctions.

### Short-term outlook:

Key data	Date	Time (NZST)	Market expects
Q1 Current Account (% of GDP)	23/6	10.45 am	-2.7%
Q1 GDP qoq	24/6	10.45 am	0.5%
May Merchandise Trade \$m	25/6	10.45 am	+835
NBBO Business Outlook	28/6	3.00 pm	-

**Comment:** Local data will be in the spotlight this week, with market focus on the Q1 GDP outturn, with market expectations centred on 0.5%. Australian data take a break next week. However, US markets will be busy with the FOMC decision and a range of data to digest. Offshore sentiment will remain a key driver in NZ markets, particularly news relating to Europe.

**Medium term outlook:** [\[Last Quarterly Economic Forecasts\]](#)



- The RBNZ began removing monetary policy stimulus at the June meeting with a 25 basis point OCR increase. In addition, the RBNZ indicated it will look to continue to increase the OCR over the coming year as economic and financial market conditions allow.
- The RBNZ left its projection for the 90-day interest rate broadly unchanged at the June MPS. It continued to note that higher bank funding costs, upward slope of the yield curve and the fact that a greater proportion of borrowers are now on floating rate mortgages will "reduce the extent to which the OCR will need to be increased relative to previous cycles". This is in line with our expectations that OCR increases will be in 25 basis point increments this year and eventually peak at 5%.
- The RBNZ forecasts headline CPI inflation to peak at 5.3% in June 2011, boosted by a raft of Government policy changes including tobacco excise tax, the implementation of the Emissions Trading Scheme and increase in GST to 15%. We expect these changes will boost headline inflation to a peak of 5.7%, and see upside risks to the RBNZ's key assumption that medium-term inflation expectations will remain anchored. This is in light of the fact that two year ahead inflation expectations are already elevated at 2.8%.
- The RBNZ has revised down its NZ economic growth outlook slightly and explicitly notes that if the Eurozone situation deteriorated the main impact on NZ would be via higher bank funding costs. We are less optimistic than the RBNZ that the recent strength in NZ export commodity prices will continue.
- We expect that the OCR will be increased by 25bp at each meeting until the OCR reaches 5%. Given continued uncertainty in the European economy, markets are currently pricing in some risk of a pause at some point in this cycle.

## NZ Data Preview: a look at the week ahead

Data	Date	Time (NZST)	Previous	Market expects	ASB expects
Q1 Current Account - % of GDP	23/6	10.45am	-2.9	-2.7	-2.5
Q1 Gross Domestic Product - qoq	24/6	10.45am	0.8%	0.5%	0.5%
May Merchandise Trade Balance - monthly	25/6	10.45am	656m	870m	700m
June NBNZ Business Outlook - headline	28/6	3.00pm	48.2	-	-

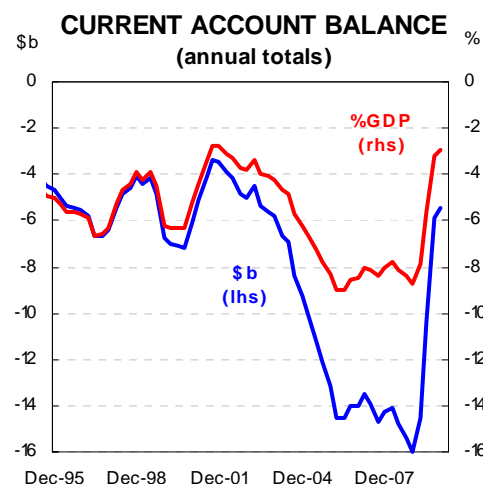
### Wednesday 23 June

#### Q1 Current Account

**previous -2.9% of GDP, m/m f/c -2.5% of GDP**

New Zealand's current account position continues to benefit from cyclical adjustment. The current account deficit shrank from over 8% of GDP to just fewer than 3% in 15 months. Behind the smaller deficit, the recession in NZ triggered a sharp drop in import demand which resulted in the trade balance moving from deficit into surplus. Meanwhile, weak business profitability (particularly in the banking sector) saw the investment income deficit reduce.

For Q1, we expect a further decline in the current account deficit, to 2.5% of GDP. The trade balance is likely to remain in surplus. Import demand remains subdued, while export receipts have increased on stronger prices. In addition, the investment income deficit is likely to remain small compared to pre-recession levels. NZ business profitability, while improving, is still affected by the recession.

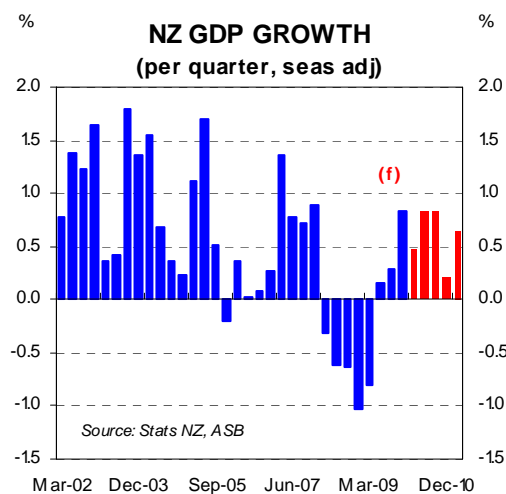


### Thursday 24 June

#### Q1 GDP

**Previous +0.8%, f/c +0.5%**

We expect GDP increased 0.5% over the March quarter, thus marking the fourth quarter of economic expansion. The economic recovery continues to gain traction and become more broad-based. In particular, we expect this quarter's growth to be driven by further recovery in those areas most impaired during the recession, such as manufacturing (excluding food); wholesale and retail trade, and; transport, storage and communication. However, over Q1 we expect a few pockets of weakness. The drought in Northland likely weighed on total dairy production over Q1. In addition, renewed weakness in the housing market will weigh on financial services.



Nonetheless, we expect the recovery in GDP growth will continue to gather momentum over 2010 with the fundamentals locking into place to support growth over the next year.

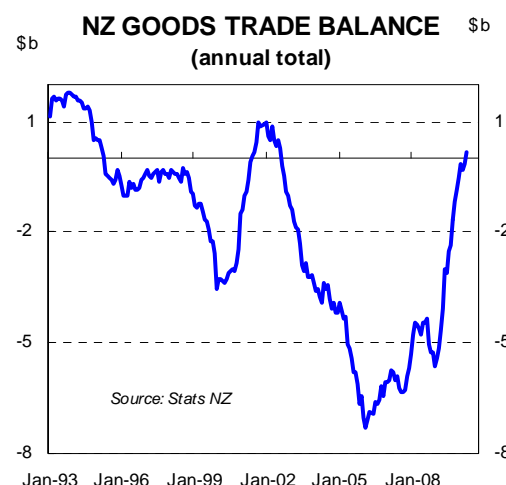
### Friday 25 June

#### May Merchandise Trade Balance

**Previous +\$656m, f/c +\$700m**

We expect a trade surplus of \$700 million in May. The trade balance tends to be stronger over the first half of the year, as agricultural exports reach the seasonal peak.

Export receipts continued to fare well through the peak agricultural season. In particular dairy receipts held up despite the drought affecting production in the top of the North Island. Dairy prices continue to improve as global supply remains tight, particularly in recent months. Meat export values are also performing well, although prices received are disappointing. Meanwhile, import demand continues to gradually recover.



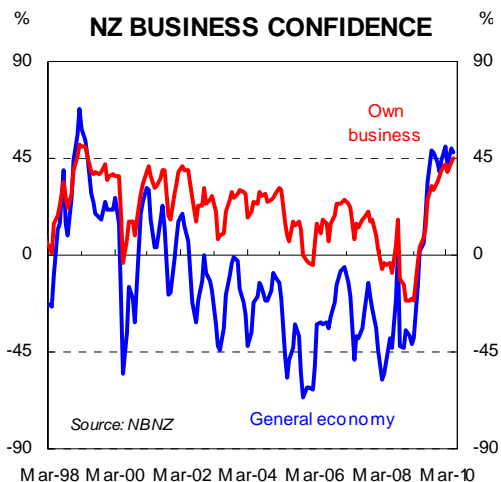
Monday 28 June

### June NBNZ Business Outlook

Previous: headline 48.2, own activity 45.3

There has been a substantial improvement in business sentiment over the past year. Encouragingly, businesses are feeling more confident about their own trading conditions such that they are planning for an expansion of operations. This improvement in investment and hiring intentions has begun to flow through to a rebound in plant and machinery investment and employment growth.

We expect business confidence will remain high, as demand continues to improve. However, the increase in GST on 1 October and continued slowing in housing market momentum may bring some uncertainty into the extent to which demand recovers. Pricing intentions will be an important indicator to watch for the degree of inflation pressures building up in the economy.



## NZ Data Review: weekly recap

### May REINZ House Sales

The housing market remained very subdued in May, as expected. Leading up to the Budget (20th of May), the Government had signaled its appetite to introduce changes to the tax policy around investment property. As a result, housing market activity has been light over recent months as potential buyers remained on the sideline to await further detail.

House sales remain at very weak levels in May, down 17% on year-ago levels and easing slightly from April's levels. Budget uncertainty and looming interest rate increases were likely weighing on housing market sentiment throughout May. Reflecting the weak demand, house prices slipped 1.4% over May, although remain above year-ago levels. The median number of days to sell lifted to 42 days and is now just slightly above average levels, suggesting the balance is tipping in favour of buyers. Fresh listings remain very low. However, with demand also very subdued, total housing supply remains around average levels on the Auckland market, and slightly above average on a nationwide basis

### Q2 WMM Consumer Confidence

Consumer confidence lifted over Q2, with a broad-based recovery across New Zealand. Encouragingly, the own activity index made a firm recovery, now up net positive 11% from +2.7% previously, indicating a firm lift in consumer spending over the months ahead.

There was an improvement in households' perceptions of their current financial position from a year ago to net -14% from -22%. Although that represents some improvement, households still feel worse off compared to a year ago, a feature that has likely been weighing on spending on big ticket items to date. However, households are increasingly confident about the future, with net 16% expecting their financial conditions to improve over the next year. The prospect of tax cuts appears to be providing a boost to confidence.

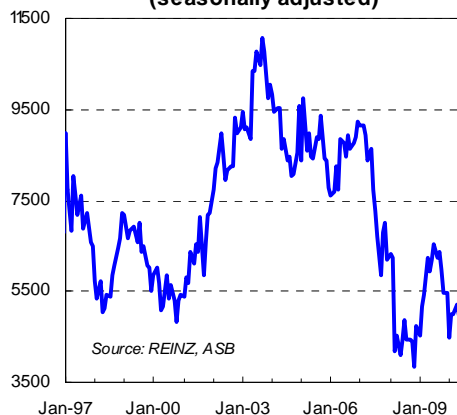
We expect the improvement in the labour market and eventual pick up in wage growth will support consumer confidence over the next year.

### May International Travel and Migration

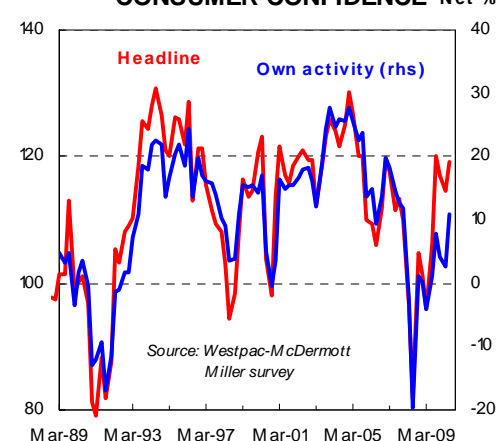
Net migration over May was very weak, with a net inflow of just 250 people recorded, following a subdued net 750 increase in April. We had anticipated the pace of net migration would slow over 2010. However, data over recent months suggest this slowdown is happening much faster than anticipated. The weaker pace of new migration can be attributed to both a decline in arrivals as well as a pick up in departures.

Short-term visitor arrivals picked up 1% over the May month. However, looking through the monthly volatility Statistics NZ note that the underlying trend appears to be declining after peaking in November 2009. In particular, the number of Australia visitors appears to be tapering off, albeit from reasonably high numbers. Encouragingly, the recovery in Asian visitor arrivals appears to be continuing. However, visitor arrivals from the UK and US continue to decline.

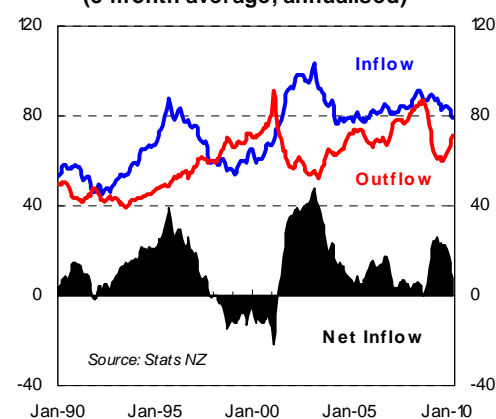
No. MONTHLY DWELLING SALES (seasonally adjusted)



Index CONSUMER CONFIDENCE Net %



'000s NZ MIGRATION (3-month average, annualised) '000s



## Global Data Calendars

Note: Calendar 2 is in UK times. Add 11 hours for NZ times.

### Calendar - Australasia, Japan and China

Date	Time		Econ Event	Period	Unit	Forecast			
	NZT					Last	Market	ASB/CBA	
Mon 21 Jun	16.30	JP	All industry activity index	Apr	m%ch	-0.8	~	~	
Tue 22 Jun	13.30	AU	New motor vehicle sales	May	m%ch	8.4	~	~	
					y%ch	28.7	~	~	
	15.00	NZ	Credit card spending	May	m%ch	-1.2	~	~	
					y%ch	1.9	~	~	
Wed 23 Jun	10.45	NZ	Current account balance	QI	\$bn	-3.6	-0.25	~	
	10.45	NZ	Account deficit-GDP ratio	QI	%	-2.9	-2.7	-2.5	
Thu 24 Jun	10.45	NZ	GDP	QI	q%ch	0.8	0.5	0.5	
					y%ch	0.4	1.8	1.8	
	12.00	AU	Conference board leading index	Apr	m%ch	0.3	~	~	
	11.50	JP	Corporate service price index	May	y%ch	-1.1	~	~	
	11.50	JP	Merchandise trade balance	May	¥bn	729.1	723.5	~	
Fri 25 Jun	02.00	NZ	NZ All Whites vs. Paraguay	-	-	1:1	-	-	
	10.45	NZ	Trade balance	May	\$mn	656.0	767.0	700.0	
					ytd	161.0	0.0	~	
		11.30	JP	National CPI	May	y%ch	-1.2	-1.1	~
		13.30	AU	Financial accounts	QI	~	~	~	~
	14.00	CH	Industrial profits	May	ytd y%ch	119.7	~	~	

## Calendar – North America & Europe

Please note all days and times are UK time, not local release day/times

Date	UK			Period	Unit	Last	Forecast	
	Time	Econ	Event				Market	CBA
Tue 22 Jun	~	UK	U.K. Budget report published	Jun	~	~	~	~
	09.00	EZ	ECB Euro-Zone current account	Apr	€bn	1.7	~	~
	09.00	GE	IFO	Jun	Index	~	~	~
	12.00	CA	CPI	May	m%ch	0.3	~	~
	15.00	EZ	consumer confidence	Jun	Index	-18.0	~	~
	15.00	US	Richmond Fed manufacturing index	Jun	Index	26.0	21.0	~
	15.00	US	Existing home sales	May	\$mn m%ch	5.8 7.6	6.2 7.5	~ ~
	15.00	US	House price index	Apr	m%ch	0.3	~	~
Wed 23 Jun	07.00	GE	GfK consumer confidence survey	Jul	Index	3.5	~	~
	08.30	GE	PMI services	Jun	Index	54.8	~	~
	08.30	GE	PMI manufacturing	Jun	Index	58.4	~	~
	09.00	EZ	PMI services	Jun	Index	56.2	~	~
	09.00	EZ	PMI manufacturing	Jun	Index	55.8	~	~
	09.00	EZ	PMI composite	Jun	Index	56.4	~	~
	09.30	UK	Bank of England minutes	Jun	~	~	~	~
	13.30	CA	Retail sales	Apr	m%ch	2.1	~	~
	15.00	US	New home sales	May	'000 m%ch	504.0 14.8	410.0 -18.7	~ ~
	19.15	US	FOMC rate decision	Jun	%	0.25	0.25	~
Thu 24 Jun	10.00	EZ	Industrial new orders	Apr	m%ch	5.7	~	~
	13.30	US	Durable goods orders	May	%	2.8	-1.5	~
	13.30	US	Durables ex transportation	May	%	-1.1	1.0	~
	13.30	US	Initial jobless and continuing claims	Jun	~	~	~	~
Fri 25 Jun	13.30	US	GDP (annualized)	Q1	q%ch	3.0	3.0	~
	13.30	US	Personal consumption	Q1	q%ch	3.5	~	~
	13.30	US	GDP price index	Q1	q%ch	1.0	1.0	~
	13.30	US	Core PCE	Q1	q%ch	0.6	~	~
	14.55	US	Uni of Michigan confidence	Jun	Index	75.5	75.4	~

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